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STATE TREASURER OF OHIO

**Ohio Constitutional Modernization Commission
Committee on Finance, Taxation, and Economic Development**

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1:30 PM

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Testimony of Seth Metcalf

Deputy Treasurer & Executive Counsel

INTRODUCTION

Chairman Cole and members of the Finance, Taxation, and Economic Development Committee - good afternoon. Thank you for the opportunity to appear before you on behalf of State Treasurer Josh Mandel. As you may recall, I provided testimony before this Committee on May 8, 2014 regarding the historical development of Article VIII of the Ohio Constitution and the Sinking Fund Commission, the current mechanisms for funding debt in this state and certain potentially obsolete sections of Article VIII. It is an honor to appear before this Committee for a second time.

Today, my testimony will address two topics. First, I would like to build upon my remarks from my last time before the Committee. Whereas on that occasion I focused more on the history of Article VIII and the Sinking Fund Commission, today I will address the continuing need to modernize Article VIII and highlight potential options to accomplish that goal. Second, I will provide a brief overview of OhioCheckbook.com as part of the ongoing Treasurer's Transparency Project.

Following each topic, I would like to provide an opportunity for questions, so that we may have a more focused discussion on each topic separately.

THE MODERNIZATION OF ARTICLE VIII

As you know, Article VIII of the Ohio Constitution concerns the public debt of the state. At its core, Article VIII really serves two functions: first, it authorizes Ohio to incur debt with certain limitations, and second, it sets forth the mechanism by which Ohio issues and pays its debt. While this underlying framework has remained intact since its enactment in 1851, Article VIII has grown tremendously over that time—both in length and complexity.

As a result, Article VIII is by far the largest article in the Constitution, and, in fact, it now constitutes just under one-half of the entire Constitution. Unfortunately, with this growth has come a corresponding reduction in the transparency of the debt issuance process at the constitutional level. Perhaps even more troubling is the fact that as Article VIII has grown, the safeguards put in place by the framers of the Constitution have gradually been eroded. However, for as complicated and convoluted as Article VIII has become, the solutions are equally simple.

Article VIII's Fundamental Defects

Article VIII has two fundamental defects. The first is the \$750,000 debt limitation that has existed since its birth. Section 1 of Article VIII permits Ohio to contract debts, but it expressly limits the amount of this debt to a total of \$750,000. To provide some context, in 1851, the state's general revenue expenditures totaled approximately \$1.64 million. For comparison's sake, in 2014, Ohio's general revenue expenditures totaled approximately \$28.9 billion. Given this growth in the Ohio economy since 1851, the \$750,000 debt limitation has become antiquated. Ohio needs the ability to borrow more than \$750,000.

That leads us to the second problem with Article VIII—the so-called “cure” for this disease, which has been applied in the form of inconsistent and highly complex amendments to Article VIII. In section 2 of Article VIII, the framers of the Constitution initially carved out an exception to the \$750,000 debt limitation, permitting the state to contract additional debt but only to “repel invasion, suppress insurrection, defend the State in war, or to redeem the present indebtedness of the State . . .” Rather than addressing the outdated \$750,000 debt limitation head-on, over the past 70 years, section 2 has instead been amended eighteen (18) times to provide specific exceptions to the debt limitation, becoming a cancerous growth on the Constitution. A strong case can be made that the cure has now become worse than the disease.

The Consequences of Repeatedly Amending Section 2 of Article VIII

While the intentions behind these amendments were undoubtedly good, they have had significant consequences. As an initial matter, the amendments to section 2 have rendered the debt limitation in section 1 entirely meaningless. As of June 30, 2014, the state's total indebtedness was approximately \$10.93 billion. I don't highlight that figure to suggest that it is an unhealthy amount of debt; rather, it simply demonstrates how meaningless the \$750,000 debt limitation has become. The amendments have effectively removed any overall debt limit. The exceptions have swallowed the rule.

Another problem with the patchwork of exceptions is that they have made Article VIII nearly incomprehensible. The voluminous language obfuscates the fact that there is, for all intents and purposes, no longer an overall debt limitation. Exhibit 1 in your packet outlines in a chart form the debt authorizations that have been provided for in Article VIII. You can see from the chart

that, in addition to simply continuing to amend section 2 to permit the incurrence of debt in excess of \$750,000, there has also been a progression in how the state sought to limit these new debt issuances. In the earlier amendments, the authorization provided for a “maximum par.” Later amendments provided for a “maximum outstanding,” and then an “annual maximum.” Although these amendments illustrate a continuing effort to balance appropriate controls on the state’s debt with the state’s need for flexibility in its borrowing, they have also made Article VIII unintelligible. As a result, transparency has been limited and the people’s ability to effectively exercise their role as overseers of government action has been hampered.

The growth in exceptions has also further undercut another of the framers’ intended safeguards: the Commission of the Sinking Fund. Sections 7 through 11 of Article VIII created the Sinking Fund and the Commissioners of the Sinking Fund, and set forth their respective functions and responsibilities. As I discussed in my last testimony, all debts of the State of Ohio were originally to be paid from the Sinking Fund. The Commission of the Sinking Fund, which includes the five statewide executive officeholders, was then tasked with interpreting the legal authorization to issue debt for the State of Ohio, implementing it, ensuring repayment, and producing a biennial and semiannual report. However, many of the amendments to section 2, pursuant to which a significant amount of the state’s current outstanding debt has been issued, permit this check to be circumvented. Under those amendments, the responsibilities of the Commission of the Sinking Fund are delegated to either the General Assembly or the Ohio Public Facilities Commission, thereby transferring accountability of the state-wide executive officeholders from the Constitution to statute. The Commissioners of the Sinking Fund have not even met since March of 2008.

Potential Solutions to Address the Fundamental Defects in Article VIII

If Article VIII is to include a meaningful overall debt limitation—consistent with the conservative approach to debt of the framers of the Ohio Constitution—this Commission can look to existing section 17 of Article VIII for guidance. Section 17 was enacted in 1999, and it prevents the state from issuing any debt if payment of debt service on direct obligations of the state would “exceed five percent of the total estimated revenues of the state for the General Revenue Fund and from net state lottery proceeds. . .”

Section 17 places a limitation on the annual debt service of the state. It does this on a percentage basis, which will allow it to remain effective regardless of future growth in the state’s economy. What it does not do, however, is limit the state’s total outstanding indebtedness. In recent times, Ohio has elected to pay its debt over relatively short periods of time—for the most part, over no more than twenty years. Not everyone takes this approach. The Ohio State University, for example, issued century bonds that will be paid off, as their name indicates, over a 100-year period. If the state were to adopt that approach in the future, the state’s overall debt load could increase significantly, with its annual debt obligations only increasing marginally. The 5% limitation in Section 17 is not effective in controlling that type of borrowing. For that reason, an overall debt limitation makes sense.

To make the debt limitation in section 1 meaningful again, it should be replaced with a percentage-based limitation, like the one in section 17. I am not here to suggest a particular percentage, but for comparison’s sake, in 1851, Article VIII’s \$750,000 cap represented 46 percent of the state’s general revenue expenditures at the time. Today’s debt of \$10.93 billion

represents approximately 38 percent of the state's general revenue expenditures. Regardless of where the percentage is fixed, it would be a far more meaningful limitation than the current \$750,000 cap.

A percentage-based limitation would also have the added benefit of rendering the numerous exceptions to the \$750,000 cap unnecessary. The length and complexity of Article VIII could be reduced significantly. As the 1970's Commission recognized, a provision would simply need to be added that assured the continued validity of all obligations issued under the current Article VIII.

If section 2 and its numerous amendments were excised, I would like to note that it would be worthwhile to at least maintain the titles of these sections in Article VIII for historical purposes. Section titles that should be retained include, for example, the authorization for the issuance of debt to raise funds to compensate veterans from World War II, the Korean War, and Vietnam. Ohio may no longer need to issue debt for those purposes, but there will be wars in the future, and Ohio would be well served to at least preserve these reminders of our historical tradition of taking care of our veterans.

The other safeguard that has gradually been lost—the role of the Sinking Fund Commission—could easily be restored as well. In our view, there is real merit to involving the five statewide executive officeholders in the debt issuance process. They provide another valuable check on the state's incurrence of debt. The easiest and most logical way of reinstating this safeguard is to replace all references to the Sinking Fund Commission—which uses the outdated phrase “sinking fund”—with references to the Ohio Public Facilities Commission—which is an active organization involved in the debt issuance process, of which all of the statewide executive officeholders are currently members.

Overview of Other Ideas to Modernize Article VIII

Today, I wanted to address what, in the view of the Treasurer's office, are the fundamental defects in Article VIII. However, there are a number of other improvements that could be made to modernize and improve the functioning of Article VIII. Without delving into any of these ideas in great detail, I wanted to briefly touch on a few.

The two percentage-based debt limitations I've discussed—one for total indebtedness and the other for annual debt obligations—would apply only to direct obligations of the state and would not, however, apply to a borrowing such as a conduit issuance. A conduit issuance is not a direct obligation of the state and, therefore, does not deserve a constitutional limitation.

An important consideration for this Committee should be the extent to which the Constitution permits the General Assembly to incur debt for generic purposes. The 1851 Constitution delegated this discretion to the General Assembly. However, a good case can be made for limiting the incurrence of such debt only for the purpose of “permanent improvements.” This would increase transparency and prevent the General Assembly from simply appropriating funds for generic purposes. However, to be consistent with Ohio's history, exceptions should be identified for veterans bonds and economic development purposes or other “non-permanent improvements” based on, perhaps, a super-majority vote of the General Assembly.

A single section of Article VIII should generally permit conduit issuances that are not direct obligations of the state. As such, neither the overall debt limitation nor the annual debt service limitation would apply. This would condense sections 13, 14, and 16 into a single section, further simplifying Article VIII.

Finally, given the fact that the administrative functions of the Sinking Fund Commission, including the financial reporting regarding state debt, have already been transitioned to the Treasurer's office, it would make sense for the Constitution to formally recognize that the Treasurer's office administers those duties.

Conclusion

As originally adopted in 1851, Article VIII reflected the framers' conservative and cautious approach to debt. The original drafters included specific safeguards to ensure fiscal responsibility—namely, an overall debt limitation and the involvement of the five statewide executive officeholders in the debt issuance process. Over time, in attempting to work around section 1's outdated \$750,000 debt limitation, these safeguards were unknowingly abandoned. The problem with section 1 is not that it imposes an overall debt limitation. Rather, the problem with section 1 is that it contains a debt limitation that is a fixed number that has not grown with Ohio's economy. That defect can easily be remedied by reinstating a meaningful limitation, such as in a percentage form. This simple fix, coupled with updating the name from the "Sinking Fund Commission" to the "Ohio Public Facilities Commission," would result in a more streamlined, transparent, and effective Constitutional governance of state borrowing.

Thank you for the opportunity to present to the Committee today. At this time, I would be happy to answer any questions on this section of my testimony.

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TRANSPARENCY AND OHIOCHECKBOOK.COM

Now I would like to provide the Committee with a brief overview of the Treasurer's Transparency Project and the new initiative that Treasurer Mandel recently undertook to display the State of Ohio's checkbook online.

As one of the first initiatives of his administration, Treasurer Mandel launched the Treasurer's Transparency Project in 2011 to shine sunshine on the inter-workings of state government. By leveraging advancements in technology, the Transparency Project allows taxpayers and citizens enhanced visibility and greater access into how their tax dollars are being spent.

This project has evolved over the years. Currently, the Treasurer's office maintains searchable databases displaying salaries of state and education employees, interactive state property maps, and county investment reports. The State Library of Ohio recently partnered with our office to present an online compilation of the state's Annual Reports published by the Treasurer's office since the early 1800s.

In December 2014, Treasurer Mandel launched OhioCheckbook.com, a cutting-edge website that sets a new national standard for transparency. This website takes all state spending, from a multi-million dollar road expenditure to a two dollar office supply expense, and places it all online for the first time in Ohio history.

OhioCheckbook.com includes more than \$408 billion in state spending spanning seven fiscal years. It displays more than 112 million individual transactions, and approximately 3.9 billion unique pieces of information. We believe that our initiative sets a new national standard for transparency because of the level of financial data provided, and because it is built to be user-friendly and intuitive.

Instead of just displaying rows and columns of data, OhioCheckbook.com features a powerful "Google-style" contextual search engine. It presents spending information through fully interactive charts that allow users to drill down and compare state expenses like never before.

If you find an expense that is interesting, we have fully integrated the website with social media networks, empowering users to share charts and checks, as well as with the capability to contact agency fiscal officers with questions.

The reason I mention this initiative today is because as we talk about modernizing our Constitution, we should also acknowledge changes being made inside of our government. We believe that this initiative places Ohio as the leader of the national movement toward a more open and responsive government.

I have included a presentation packet previewing OhioCheckbook.com and its various features. Our office would gladly schedule demonstrations with the members at your convenience.

Thank you again for the opportunity to present to the Committee today. At this time, I would be happy to answer any questions on this section of my testimony.

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